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C O N F I D E N T I A L SECTION 01 OF 03 QUITO 001715

SIPDIS

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TAGS: [PGOV](#) [PREL](#) [EFIN](#) [ENRG](#) [EC](#)

SUBJECT: ECUADOR: MIXED SIGNALS ON CHAVEZ DEAL

REF: A. SECSTATE 127251

[1](#)B. QUITO 1663

Classified By: Charge d'Affaires AI Kevin Herbert, for reasons 1.4 (b&d ).

[1](#)1. (C) Summary: Press reports suggest Ecuador is ready to sign agreements with Venezuelan President Hugo Chavez on financing and oil deals, despite President Alfredo Palacio's public denials that any GOE decision has been taken. Privately, however, Palacio administration officials are telling us a different story. Unfortunately, the most public advocate of cutting deals with Venezuela, Minister of Economy and Finance Rafael Correa, has not been clearly refuted in public or reined in by President Palacio, fueling uncertainty. Since prospects for multilateral financing appear dim, it is natural that Correa, already ideologically committed to state-controlled economies and no fan of the international financial institutions (IFIs), would welcome a financing offer from Chavez. More rational members of the Palacio administration are looking for viable alternatives to Chavez. With the notable exceptions of Foreign Minister Parra and Correa, we do not believe the GOE is eager for closer relations with Chavez. Still, the GOE will want to maintain cordial relations with its Andean neighbor.

[1](#)2. (C) Given local sensitivities to USG pressure, we have refrained from public comment on these developments. Privately, we have expressed to GOE interlocutors USG concerns about dealing with Chavez, drawing from existing guidance (Ref A), and urged more definitive actions on Ecuadorian-Venezuelan relations. We will have an opportunity to meet directly with Palacio on July 27. Meanwhile, we will work quietly with the anti-Chavez forces to blunt the effect of Correa, until Palacio decides to jettison him, as he is apparently considering doing to the Foreign Minister as early as next week. End Summary.

IFI Financing Delayed, at Best  
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[1](#)3. (C) Disbursements from the World Bank (WB) and Inter-American Development Bank (IDB) have been put on hold, pending an evaluation from the IMF. An IMF team is expected to arrive in Ecuador August 22. However, Correa said he intends to meet with the IMF to press Ecuador's case when he is in Washington for the IDB meetings the week of July 25.

[1](#)4. (C) We learned from IDB sources on July 19 that the Ministry of Economy sent letters last week to the IDB, WB, the Andean Community Development Bank (CAF) and the Spanish Embassy announcing significant cuts in their programs (up to 50% in the case of the IDB). Apparently, Correa wants only funds with no strings attached (i.e., neither loans or grants with conditions). Given this posture and previous comments critical of the IFIs, it is difficult to believe that Correa is sincere about working with the IFIs.

Searching for Alternative Financing  
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[1](#)5. (C) With dim prospects for financing from the IFIs and virtually no chance at attracting private financing, given the political and economic uncertainties in the country, it is not surprising that Correa (a likely 2006 presidential candidate) would seek funding elsewhere. His first stop was Venezuela, but he has also mentioned China, Brazil and the Latin American Reserve Fund as other possible financing sources.

[1](#)6. (C) An ideologue, with no political or government experience, Correa tends to view things from an academic, rather than political or practical perspective. Thus, Chavez' offer for financing with no strings attached (at least according to Correa) must look attractive to him. Worse still, Correa identifies more with Chavez' statist policies than with IFI positions and current generally accepted economic policies. (See reftel A, Quito 1181, regarding Correa's tendency to let his ideology override his intelligence.)

Talking But No Deals Yet  
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[1](#)7. (C) Correa sent six operatives July 19, including Vice Minister of Finance Magdalena Barreiro, to Caracas to work on

technical aspects of the possible bond purchase. Correa said he intends to replace expensive short-term internal debt (CETES, with interest rates of 8.5%) with long-term (minimum 3 years) debt at lower interest rates. He has not provided any other details on the proposal.

18. (C) When the possibility of Venezuelan financing first hit the press, Correa denied it, stating he was in Caracas to talk energy policy (Ref B). Subsequently, there were reports about the possibility of Venezuela refining Ecuadorian oil. Press reports from the July 18 meeting of Andean leaders noted that Chavez made a similar unrealistic proposal to the Andean leaders, the creation of "Petroandina," a regional oil consortium. Following his meeting with Chavez, President Palacio made no mention of the Venezuelan bond, refinery or Petroandina proposals.

19. (C) EmbOffs met with Energy Minister Ivan Rodriguez on July 20 to get his views on the Venezuela-related oil proposals. Rodriguez took umbrage at Correa's messing in oil policy. He added that Palacio had little in common with Chavez and Rodriguez thought it unlikely that Palacio would want closer relations with him. EmbOff's noted that the public perception was much different. Rodriguez referred EmbOffs to the July 20 "El Universo" front-page story where Palacio said there was nothing agreed to with Chavez. That, Rodriguez said, was the true story.

10. (C) As to Chavez' offer for assistance in the oil sector, Rodriguez said that they would look at what Chavez had to offer. Their first level of analysis would be to "look at the numbers." Then, there were political considerations to take into account, if the numbers made sense. Rodriguez said that he had resisted Venezuelan invitations to visit Caracas. He added that the GOE would welcome alternatives to the Chavez proposals. EmbOffs agreed to work with Rodriguez, particularly with respect to his plans to modernize PetroEcuador's refinery in Esmeraldas. (More on that meeting in SepTel.)

#### Palacio and Herreria Against the VZ Plan -----

11. (C) In a July 19 meeting with Charge and ADCM, Presidential Advisor Herreria said that Correa was acting on his own, without authorization from Palacio. Charge acknowledged Ecuador's financing needs, but said the GOE needed to carefully weigh the political and economic costs of the financing. Charge also noted that recent GOE actions made it appear that Ecuador was drawing itself closer to Venezuela. Noting our concerns with Chavez' policies, he called for the Palacio administration to clarify its position with respect to Venezuela.

12. (C) Herreria said he would recommend that Palacio demonstrate that he is not pro-Chavez by declining an invitation to attend Bolivarian celebrations sponsored by the Venezuelan Embassy on July 24. In addition, when in Guayaquil next week, Palacio would make clear that Ecuador is not subject to any country's influence, including Venezuela. According to Herreria, Palacio realizes Correa has designs on the presidency, but that in the end Palacio will not support a bond deal with Chavez. He did not explain why Palacio has not reined in the charismatic Correa.

13. (C) As to Foreign Minister Parra, Herreria said Palacio was fed up with him. In a subsequent July 20 phone call to ADCM, Herreria said Palacio intended to dump Parra, as soon as next week, with a couple of other ministers. Curiously, while Palacio, according to Herreria, described Correa as "dangerously esoteric," Correa was not mentioned as one of those to be dismissed from the cabinet. However, Palacio did agree to invite Embassy leadership to a private meal on July 27 to hold frank discussions, with an open agenda.

#### Comment -----

14. (C) Correa is clearly a loose cannon that Palacio eventually must come to terms with, but we are not the ones to tell him so, at least directly. Still, despite press reports, the GOE is not ready to enter into any agreement with Chavez. However, any public statements from the USG to pressure the GOE to stay away from Chavez could have the opposite effect. A common theme throughout our conversations and indeed much of the public rhetoric of this administration is that Ecuador is a sovereign nation capable of running (or, just as likely, ruining) its own affairs. We must also be judicious in our private comments to GOE officials for the same reason. This is still an administration and President looking for acceptance and legitimacy, given its irregular ascension to power.

15. (C) Energy Minister Rodriguez, with whom we believe we can work, astutely noted that the GOE is looking for viable alternatives to offers such as those from Chavez. That is not to say that we should change our position that Ecuador

should adopt sound and sustainable economic policies as a precondition to further IFI support. However, there are other avenues to pursue. Facilitating interactions between the GOE and the U.S. private sector, offering technical assistance and visits by high-level USG officials or a presidential emissary are among the actions we can take to lend legitimacy to Palacio, which he clearly craves.

16. (C) Next month's arrival of Ambassador-designate Jewell will provide new impetus to our bilateral relationship. In the interim, the proposed July 27 meeting between Embassy leadership and President Palacio presents another opportunity to make our case directly with Palacio. We will also focus on those within the administration with whom we can work, including Minister of Trade Molestina, Minister of Energy Rodriguez, and Presidential Advisor Herreria.  
HERBERT